

SF tips Smaller Companies **Gold** Fund

Newsletter - Issue 31, November 2011

Kebabbed - By Ross Jones & Tom Winnifrith



In the early hours of Thursday 27th October Euro leaders delivered the 'blockbuster' package which was set to lead the way out of the EU debt quagmire. French President, Sarkozy, said that after a long debate leaders had reached an agreement with private banks on a 'voluntary' 50% reduction of Greece's debt and that EU banks subsequently needed to clear a 9% tier one capital hurdle after marking to market sovereign bond books. As a response it was also agreed that the European Financial Stability Facility will be leveraged, with the suggested expansion resulting in the bailout vehicle having its firepower increased by four to five times. The funds for this are likely to be sourced by tapping sovereign wealth funds and Chinese cash. The exact details are yet to surface, but any potential Chinese involvement (and there is no guarantee that the Chinese will play ball) is sure to come with a catch. We will almost certainly see a revival of the demand for open door access for Chinese firms keen to invest in EU industry and for an end to the EU's veto on China's full market status.

In addition to the 50% haircut, which is stressed as being voluntary so therefore does not trigger a credit event and subsequent CDS payout (which was cleverly worded like this to ensure this exact outcome but has made a mockery of the International Swaps and Derivatives Association), and the expanded bail out fund, remaining Greek debt is set to be refinanced at preferential rates and moving forwards the naughty

child Greece will be 'supervised' even more closely to ensure adherence to its austerity program. That is a programme which will see Greek GDP/Debt ratios back to 120%. Er... by 2020 if all goes well. It was also agreed that, in between punch ups, Italian MPs would deliver a specific budget and deficit program to attempt to stop the country slipping into the same black hole as Greece.

What this ultimately means is that the EFSF could provide guarantees for anywhere between EUR1 – 1.4 trillion of bonds issued by member countries, notably Spain and Italy. But if France was to lose its AAA rating, as has been warned, even this revised plan will not be adequate as it would, *ceteris paribus*, reduce the effective lending capacity by France's share of the guarantees. The issue is that the risk profile of France changes dramatically with its involvement here. Critics have already suggested this and have drawn similarities between the concentrated risks involved with CDOs back in 2007/2008. But despite this, the EFSF expansion was given the market's approval, with bank shares leading the way.

But it does not look like Greece is going to play ball and with the country's decision to call a referendum on the 5 day old bailout everything is up in the air again and all bets could in fact be off here as there is a real chance the country could detach itself from the rest of the region, in a monetary sense.

But assuming the Greek people play ball the headline 50% hair cut was not actually all it seemed. It is likely this will be some sort of NPV adjusted figure, but in real terms Greece has EUR350 billion in total debt, which includes EUR70 billion of 'Troika loans' which will not be chopped up. Strip this out, and of the EUR280 billion remaining it is estimated that circa EUR75 billion is held by the ECB and like the first elite tranche, this EUR75 billion will also remain untouched. So, strip out the elite loans, which will not suffer any pain, and this leaves roughly EUR200 billion which will actually be cut. Out of this 200 billion it is estimated that c35% is held by Greek pension funds. So, if we strip out the 'elite loans' the total debt that will actually be cut is EUR 100 billion, of which a good deal of this is attributable to Greek pension and retirement obligations. All in all the haircut is actually only 28% of debt, with the real pain being felt by the Greek taxpayer – that is to say that the result of this plan seems to be that the haves have more (or at least what they initially had) and have nots have less... we cannot see the Greek people signing up to this.

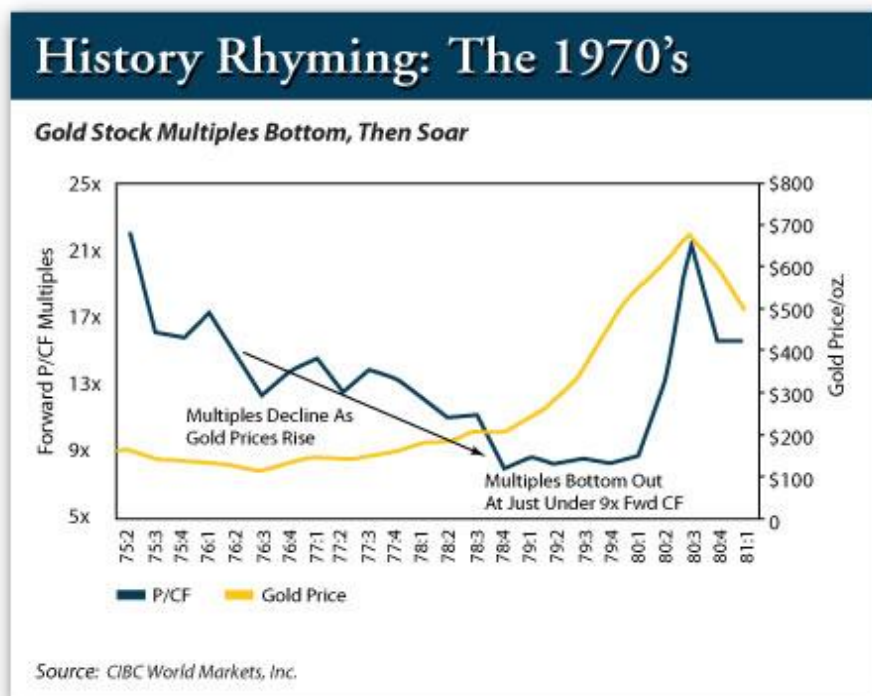
But a further issue is where will the estimated EUR106 billion come from that is needed to fill the hole in the balance sheets of EU banks? Plan A is that the banks will employ a strategy of belt tightening whilst seeking private capital to cover the short fall. It is estimated that Greek banks alone need EUR30 billion, that Spanish banks need EUR26.1 billion, and that Italian banks need EUR14.8 billion, and with this trio seen as the 'high risk club' it seems that Plan B will be pushed through sooner rather than later. Plan B means that national governments, and ultimately the EFSF will be roped in to meet the banking sector needs. However, the problem is if the EFSF is likely to be stretched whilst providing liquidity to EU countries how will it also fund the region's bank's capital shortfalls?

Our view is that the stronger operations will reach the required capital threshold by profit retention and, or scrip dividends, non core asset sales (which will see security prices fall) and ultimately capital hikes. But the weaker banks are ultimately going to have to seek government assistance or request an EFSF loan. There is also the ECB's short term funding system that has been put in place; full twelve month Euro funding or USD funding on a 3 month term, but this, in our view, is not a credible solution to the issue.

Despite investors cheering the news initially, we can see that the early morning announcement is little more than a blue print and the tough creases still need to be ironed out. Our view is that; yes the plan gave the market a day of respite and a subsequent relief rally, but the fundamental debt issues will not be solved until spending is pulled back in line and/or the weaker EU countries revert to their old currencies *a la* Iceland. Ultimately, with it currently being estimated that a 10% fall in the value of the Euro will result in a 0.6% increase in GDP, we take the view that it is not long before the ECB joins the QE club if the region is to stay united. Club membership involves the aim of dramatically lowering the value of your currency in order to inflate your way out of debt, whilst making your exports more attractive. The ring leader of the group, the US, upon issuing USD29 billion of 7 year Treasuries on Thursday 27th October 2011 pushed through 100% in regard to its debt/GDP ratio, without anyone really batting an eyelid.

Ultimately, this has to lead to runaway inflation across the West which will be good for equities as opposed to fixed income securities. But the big winner from inflation will be Gold as the only real safe haven investment as our paper currencies become worth less and less in real terms. The last time the world faced such a crisis which led directly to inflation was the second half of the 1970s. As the chart below shows, the value of gold equities initially lagged the gold price. It was only after the gold price really

started to gather a head of steam that shares in gold mining companies raced ahead, first catching up with gold and then overtaking it.



At the SF tips Smaller Companies Gold Fund, our team is convinced that 2011 is 1977. That does not mean that Malcolm Burne is sporting God Save the Queen, Sex Pistols T-shirts. It means that we reckon the pickup in gold price is only now starting to accelerate. The next few months will see unprecedented QE in the US, UK, Japan and Europe. That will, we believe send gold well past \$2000 very quickly and that could, we believe, see the prices of many gold and silver mid caps double or more. We look forward to it...

Ross Jones & Tom Winniffrith

You can download the application [form](#) from and here and the simplified prospectus from [here](#). If you have any questions please contact 01624 641 318 or email goldfund@t1psim.com.

Fund Information

Size:	£18,215,050.05 (01/11/11)
Launch date:	24 July 2009
Launch price:	£1.00
Current Yield:	0.00%
Legal Status:	OEIC
Annual Management Fee:	1.5%
Initial Charge:	5.25%
Minimum lump sum Investment:	£500.00
Minimum monthly investment:	£25.00
SEDOL code:	B3YQ855
Unit offer price:	Single Priced Fund Last Dealt Price: 152.94p (01/11/11)
Unit bid price:	As Above

Top 10 Holdings

Stock Name	Fund %
Ascot Mining	8.59
Ariana Resources	8.28
Hambledon Mining Plc	5.94
Vatukoula Gold Mines	5.02
Conroy Gold	3.42
Sovereign Mines	3.42
Cluff Gold	3.38
Chaarat Gold	2.61
Great Panther Silver	2.61
Kryso Resources	2.61

Benchmarking

Total return, bid to bid line chart from 11/09/2009 to 03/11/2011 from UKUT and OEICs Universe



Cumulative Performance 01/11/2011

	1m	3m	6m	1y	2y	Since inception
SF T1ps Smaller Companies Gold Fund	0.72	-17.26	-27.09	-6.20	50.79	52.90
Specialist	+4.1	+5.8	-7.3	1.9	9.88	17.24

Discrete Performance 01/11/2011

	0-12m	12-24m
SF T1ps Smaller Companies Gold Fund	-6.20	60.75
Specialist	-9.4	14.5

The Fund was launched in September 2009 and 3-year and 5-year performance results are not available.

Source: Financial Express

Past Performance is not a reliable indication of future results

How To Buy Gold Fund Units

1. You can deal through www.JPJShare.com at the initial fee rate of 2%.
2. Contact your broker. Most brokers offer the chance to buy units although few can match JPJShare.com's initial rate of 2%. But call your broker and give him the fund's SEDOL code: B3 YQ 855. If your broker will not deal please call Sarah Read on 01624 641318 and she will try to rectify the situation.
3. Deal directly through t1ps and The Share Centre at the initial fee rate of 2.5%. If you want an application form email goldfund@t1psim.com or go to www.t1psim.com.
4. If you choose to invest directly, once you have made an initial investment (of as little as £500) you can set up a monthly standing order with The Share Centre to drip feed further cash (as little as £25 a month) into the fund. All existing fund holders can set up such an order.

If you have any questions about investing in the SF t1ps Smaller Companies Gold Fund visit our website at www.t1psim.com or email goldfund@t1psim.com.

You can download the application form from [here](#) and the simplified prospectus from [here](#).

The News Is Actually Good... - By James Faulkner



Generally, across the portfolio the news has been pretty good. We start not with a turkey but with a rabbit in Turkey. On 17th October 2011 Turkey focused gold exploration company, **Ariana Resources** announced the completion of the core components of its Pre-Feasibility Study on the Kiziltepe sector of its flagship Red Rabbit project, located in the west of the country. The study delivered improved project fundamentals with increased in-pit resources of 118,200 ounces of Gold and 1,452,600 ounces of Silver and subsequently a slightly increased mine life, now estimated to be eight years. Targeted production of 150,000 tonnes, equating to circa 20,000 ounces of Gold a year for the first five years, is set to begin by late 2012 which will provide the company with the cash needed to explore the wider area which has the potential to host in excess of 1 million ounces of Gold equivalent. Both the Gamze Vein and the Hande Vein clearly underpin the medium term growth potential here given the continuous high grades of up to 10.7g.t (Gamze) and 7.74 g/t (Hande) the company has previously identified.

The open-pit optimisation and design, site layout, production schedule and processing plant details announced within the PFS are now unlikely to change as we approach the announcement of the Feasibility Study later this year. The mine itself will be based around one central pit located at Arzu South with feeds in from satellite pits at Arzu North, Banu, Derya, and Kepeza, and is set to operate six days a week for just over eight years and one month, as opposed to 6.9 years as was previously forecast. Grades will however decrease as the production matures, i.e three to four years out, as mining shifts to Kepez, Arzu North, Banu and Derya. But it is our view that by this time the company will have progressed its exploration and future development campaigns into other workable assets which will boost production (to 30,000 oz), the minelife (to more than 10 years) and the grades.

The plan to do this is already underway with the initiation of follow up drilling at Red Rabbit which is due to be completed ahead of the Feasibility study, which should be released towards the end of 2011 (albeit after a short delay as a result of needing a recognised local firm to design and approve the tailings storage facility). Up to 4000 metres of drilling is planned on the Kiziltepe, Kepez West, Karakavak and Kizilcukur areas of the project with work having already begun on Kiziltepe's Fidan Vein. The drilling will help to enhance the understanding of, and to better define, the mineralised structures across the project with the hope of deriving additional mill feed for the planned plant. The fact that the company has its own drill team provides material flexibility in regard to this operational progression.

Currently capitalised at £13.76 million, after a number of recent purchases in the market, your fund now owns c12% of the company. Production is set to begin late next year and at this point, for the first five years of the mine, annualised output should come in at 20,000 ounces of Gold equivalent. Ariana's claim here is 50%, so at a \$1,650 gold price (a cautious assumption), and costs of \$550 an ounce, which we have revised on recent strip ratio guidance, free cashflow should be c£7.2 million a year. On a multiple of five times, that is worth £36 million, or 14.1p a share. The upside here in terms of both mineable resource expansion and Gold price is very clear – for every \$50 on the price of Gold 0.6p a share can be added to the valuation of Red Rabbit. As we write (with gold at \$1725) that valuation has increased to 15p.

Add in the company's interest in Tigris Resources (which will IPO next year), its cash and the JV with European Goldfields (where drilling this year, all funded by European, has delivered good results), and it is supremely difficult to see how Ariana is worth less than 18p per share.

There were no real surprises when **Norseman Gold** released its quarterly progress report (Q1) for the three months ended 30th September 2011. As we already knew Gold production was down by 22% on the previous quarter as a result of all three declines underperforming due to lower average grade recoveries and staffing issues. Bullen chipped in 3,619 ounces, down 27% QoQ, Harlequin's contribution was down 22% at 4,796 ounces, but production from the OK Decline slumped by 56% to 1,268 ounces. North Royal's production however shot up 109% to 1,948 ounces and helped the miner end the quarter with project stockpiles totalling 66,000 tonnes, containing an estimated 3,600 ounces of Gold.

The quarter covered the month of August which saw Gold shoot ahead as investors fled to the metal amid financial turmoil and wider macro concerns. As a result the sale price of Gold during the quarter ranged from A\$1,381 to A\$1,765 per ounce, with an average sale price of A\$1,609 being achieved. As we have mentioned on a number of occasions previously; regardless of ounces produced Norseman's costs are fixed – that is to say that as production rises the respective cash cost per ounce falls. This is evidently attractive given the strong bull case for the price of Gold but also works against Norseman when production falters. The quarter ended 30 September 2011 is a perfect example of this, with net direct operating costs per ounce coming in at A\$1,591. This saw the company post negative EBIT of \$5.5 million. Actual operating costs however, as opposed to cost per ounce, remained in line with the previous quarter.

There can be no beating around the bush; the numbers are not pretty and ultimately the quarter ended 30th September 2011 is one best forgotten. Moving forward the company has been focusing on the employment of experienced underground operators and in general looks to be pushing on with initiatives to plug the workforce hole. In regard to production, recoveries are expected to improve through the current quarter as new personnel are employed in the underground mines and operations at the North Royal open pit continue toward the hard rock ore.

Cash at the period end stood at A\$7.5 million, excluding bullion, but approximately A\$6.1 of this is committed to cash-backed environmental bonds. In addition the loan facility provided by Red Kite had been fully drawn down. This was an issue that, could be argued, the company had not been 100% transparent about. But as we all know the cash balances as at 30th September are irrelevant as post period the company completed a conditional, materially dilutive, £6.9 million equity placing (at 5p) and a

£5.1 million convertible placement (6p) as announced on 26 October 2011.

Having been pulled off the market pending the appointment of a new NOMAD, the shares came back to life on 26th October. The stock was suspended at 10p and it was clear when the shares were readmitted at circa 5.3p, that a good deal of private investors had lost their tempers, let their emotions get the better of them, and had 'dumped' their holdings in anger. Pre-placing investors had, and have, every right to be annoyed at how this has played out and how the company has over promised and under delivered but looking at the numbers, and despite a heavily dilutive placing, the investment case here is compelling. So much so that, having participated in the placing (both equity and convertibles), we continued to buy shares in the secondary market.

We took encouragement from the return of David Steinpreis as chairman and the fact that management, through a few different vehicles, made up a good chunk of the cash raised. In addition, the company has now clearly stated that by Q3, i.e. 1 Jan 2012, it will be producing Gold at an annualised rate of 120,000 ounces. It would be a serious mistake here if the management have again over promised. But we take the view that seeing as this company will now not be able to return to the market for funding, and this really is the 'last chance', the management would not provide this guidance unless they were confident of achieving the target.

For the current quarter our view is that production will reach approximately 20,000 ounces at a reduced cost of circa \$1,100 an ounce. For the full year however, taking into account guidance, production is still expected to reach the 'golden' 100,000 ounces target. Therefore, at \$1,600 Gold and a conservatively derived \$1,000 cash cost per ounce, Norseman should be generating annualised free cash flow of £37.5 million, which placed on a multiple of 3 (plus £5 million cash, £10.2 million from warrants and reduced for £10 million of debt), equates to 22p a share, fully diluted. This is why at 5p (in the placing) and circa 6p (in the market) we have *filled out boots*.

But the upside here is clear, and currently trading at 7.23p (capitalising the enlarged company at £38.2 million), based on a wholly objective appraisal the potential rewards far outweigh the possible risks given the fact that at \$2,000/oz Gold, annual production of 120,000 ounces (Norseman does actually have the capacity to do 130-140,000 ounces), and cash costs of \$725/oz, Norseman could arguably be worth 55p per share. In our view this is now the best risk reward play in the sector.

James Faulkner

Risk Warning

The value of your investment can go down as well as up and you may not get back a significant proportion of your investment. Past performance is not a reliable indicator of future results. If you are in any doubt as to the suitability of an investment, you should seek independent financial advice. * Please remember that the tax treatment depends on the individual circumstances of each investor and may be subject to change in the future.

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